

In a proper case, those money outlays may be considered which would enable the plaintiff to alleviate his remaining non-financial loss, especially his bodily suffering and depressions.

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RESALE PRICE MAINTENANCE BY AN INTEGRATED  
FIRM: THE *McKESSON & ROBBINS* CASE

Fair-trade contracts between an integrated manufacturer-wholesaler and competing independent wholesalers were held illegal by the Supreme Court in *United States v. McKesson & Robbins, Inc.*<sup>1</sup> By a literal application of the Miller-Tydings Act,<sup>2</sup> its exemption from the general law against price fixing<sup>3</sup> was held not to apply. But the ambiguous position of the integrated manufacturer—at the same time supplier and competitor of the wholesalers with whom he contracts—suggests a more complicated problem than can be solved appropriately by a literal application of the Act.

Under the general law of price fixing, agreements to fix or maintain prices have repeatedly been said to be “illegal per se,” without differentiating between whether or not they operate within the same level of distribution.<sup>4</sup> This failure to differentiate may obscure the fact that the historical objection to “horizontal” price fixing is different from that of “vertical.” Cases holding horizontal agreements illegal usually have been concerned with actual or intended market effects,<sup>5</sup> so much so that in the absence of these determinants

<sup>1</sup> 351 U.S. 305 (1956).

<sup>2</sup> 50 Stat. 693 (1937), 15 U.S.C.A. §1 (1951), quoted in text at note 15 infra. The McGuire Act, 66 Stat. 632 (1952), 15 U.S.C.A. §45 (Supp., 1956), permits state fair-trade legislation binding non-signers.

<sup>3</sup> Price fixing occurs when two or more firms at the same or different levels of distribution determine the price at which a commodity will sell, instead of leaving this determination to the free competitive market. Fair-trade contracts (resale price maintenance) represent a vertical form of price fixing whereby one firm fixes the sales price for another firm at a different level of distribution. Horizontal price fixing occurs between firms on the same level of distribution. For general discussions on resale price maintenance consult: 1 Callmann, *Unfair Competition and Trade Marks*, c. 6 (1945); Bowman, *The Prerequisites and Effects of Resale Price Maintenance*, 22 U. of Chi. L. Rev. 825 (1955); Fulda, *Resale Price Maintenance*, 21 U. of Chi. L. Rev. 175 (1954).

<sup>4</sup> E.g., *McKesson & Robbins, Inc. v. United States*, 351 U.S. 305, 310 n.9 (1956); *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707, 720 (1944); *United States v. National Ass'n of Real Estate Boards*, 339 U.S. 485, 489 (1950).

<sup>5</sup> E.g., see *United States v. Frankfort Distilleries, Inc.*, 324 U.S. 293, 296 (1944); *Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211, 213 (1951): “We reaffirm what we said in *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 223: ‘Under the Sherman Act a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal *per se*.’” Compare *Board of Trade of Chicago v. United States*, 246 U.S. 231 (1918). Specific circumstances under which price fixing is not illegal per se have already been delineated. *United States v. Frankfort Distilleries*, supra, at 301-2 (Twenty-first Amendment gives states power to engage in or sanction price fixing on intoxicating liquors.) (Frankfurter, J., concurring).

the per se illegality of horizontal price fixing may still be regarded as a somewhat open question.<sup>6</sup> Although a vertical agreement between a supplier and his dealers is equivalent to a horizontal one in that both establish the selling price for two or more dealers on the same functional level,<sup>7</sup> the vertical agreement in addition imposes a restraint on alienation, projecting the seller's control beyond the passage of title.<sup>8</sup> Consequently, the concept of per se illegality appears to have a stronger basis for vertical than for horizontal price fixing.<sup>9</sup>

In the Miller-Tydings Amendment<sup>10</sup> to the Sherman Act Congress immunized one form of vertical price fixing, minimum resale price maintenance. While the legislative history of that Act is inconclusive,<sup>11</sup> its purpose is said to be that of allowing a manufacturer to protect goodwill, his own or that of his products, by preventing injurious price cutting on his brands.<sup>12</sup> However,

<sup>6</sup> *Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211 (1951), has been thought to establish the per se illegality of horizontal price fixing (e.g., *The Per Se Illegality of Price-Fixing—Sans Power, Purpose or Effect*, 19 U. of Chi. L. Rev. 837 [1952]). While it is true that the Court felt the evidence supported a finding of horizontal conspiracy to fix prices, it must be emphasized that the prices set were the maximum resale prices for the firms to which the conspirators sold. The Court recognized this vertical element, stating: "For such agreements, no less than those to fix minimum prices, cripple the freedom of traders and thereby restrain their ability to sell in accordance with their own judgment." *Ibid.*, at 213. Compare authorities cited note 8 *infra*.

<sup>7</sup> *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373, 407-8 (1911). Compare *Bement v. National Harrow Co.*, 186 U.S. 70 (1902), where a patentee's contract dictating the price at which his licensee-manufacturer could sell was sustained. Such a situation must be differentiated from the forbidden vertical or horizontal price fixing, for whatever the number of licensees is, the effect of such an arrangement is merely to insure the patentee his monopoly profit.

<sup>8</sup> *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 351 (1908); *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373, 404-5 (1911); *Straus v. Victor Talking Machine Co.*, 243 U.S. 490, 500-501 (1917).

<sup>9</sup> This is so because in the horizontal cases it seems probable that some relationship to market effect is necessary to bring the per se doctrine into play (note 6 *supra*), while in the vertical cases the arrangement necessarily carries with it the objection of a restraint on alienation.

<sup>10</sup> 50 Stat. 693 (1937), 15 U.S.C.A. § 1 (1951), quoted in text at note 15 *infra*. This Act, passed as a rider to the District of Columbia Revenue Bill, was characterized by its supporters as merely enabling legislation, which would free state fair-trade legislation from hindrance by the federal anti-trust laws. It was not a congressional enactment or adoption of fair trade.

<sup>11</sup> A study shows that while some legislators felt that they were protecting the manufacturer's goodwill (81 Cong. Rec. 7,487-97 [1937]), an equal number rejected this concept and felt instead that they were protecting the small retailer from predatory price practices (81 Cong. Rec. 7,495-96, 8,139 [1937]; 98 Cong. Rec. 4,896-5,026 [1952]).

<sup>12</sup> E.g., *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305, 316 (1956) (Harlan, J., dissenting); 1 Callmann, *op. cit. supra* note 3, at 450-51. But see *Broxmeyer v. Polikoff*, 39 D. & C., 224 (Pa. Ct. of Com. Pleas, 1940) (fair-trade laws designed primarily to prevent destructive price-cutting among retailers). The goodwill argument has been subjected to severe criticism. E.g., Bowman, *The Prerequisites and Effects of Resale Price Maintenance*, 22 U. of Chi. L. Rev. 825, 834 (1955).

the fact that the Act was passed in response to strong pressure from retail groups, notably the National Association of Retail Druggists,<sup>13</sup> suggests that it serves an additional purpose by legalizing an arrangement having the same effect as horizontal price fixing among retailers (or wholesalers) and providing a suitable opportunity for policing the agreement.<sup>14</sup>

The Miller-Tydings Act provides that nothing contained in Section 1 of the Sherman Act

shall render illegal, contracts or agreements prescribing minimum prices for the resale of a commodity which bears, or the label or container of which bears, the trade mark, brand, or name of the producer or distributor of such commodity and which is in free and open competition with commodities of the same general class produced or distributed by others, when contracts or agreements of that description are lawful as applied to intrastate transactions, under any statute, law or public policy now or hereafter in effect in any State . . . in which such resale is to be made or to which the commodity is to be transported for such resale. . . .<sup>15</sup>

The Act continues with the following proviso:

*Provided further*, That the preceding proviso shall not make lawful any contract or agreement, providing for the establishment or maintenance of minimum resale prices on any commodity herein involved, between manufacturers, or between producers, or between wholesalers, or between brokers, or between factors, or between retailers, or between persons, firms, or corporations in competition with each other.<sup>16</sup>

<sup>13</sup> McLaughlin, *Fair Trade Acts*, 86 U. of Pa. L. Rev. 803, 817 (1938); Grether, *Solidarity in the Distributive Trades in Relation to the Control of Price Competition*, 4 *Law & Contemp. Prob.* 375, 383-84 (1937); Grether, *Experience in California with Fair Trade Legislation Restricting Price Cutting*, 24 *Calif. L. Rev.* 640, 647-49 (1936); *Judicial Construction of Fair Trade Acts*, 49 *Yale L. J.* 145, 146-47 (1939). For a discussion of the boycott of Pepsodent by the National Retail Association of Druggists when Pepsodent dropped its fair-trade agreements, and the telegram bombardment of Congress by retail associations for passage of the McGuire Act, consult 81 *Cong. Rec.* 7,487-97, esp. 7,494, 8,138-43 (1937); 98 *Cong. Rec.* 8,830-40 (1952).

<sup>14</sup> If the manufacturer chooses to withhold his products from uncooperative distributors this surmounts a great obstacle to effective price fixing, that of adequate enforcement. Cf. *National Ass'n of Window Glass Mfg'rs v. United States*, 263 U.S. 403 (1923), where the Court sustained a multi-employer-union arrangement having the effect of reducing production, although this amounted to price fixing and the union's presence served to accomplish strict adherence to the price-fixing agreement.

<sup>15</sup> 50 Stat. 693 (1937), 15 U.S.C.A. § 1 (1951).

<sup>16</sup> *Ibid.* The exact purpose of this proviso is in some doubt since it was introduced as an amendment on the floor of the Senate, and so did not receive Committee consideration. Senator Tydings stated that the amendment was "unnecessary because the provision as now found in the bill allows none of the things which the amendment specifically eliminates. . . ." 81 *Cong. Rec.* 7,487 (1937), discussed in *Eastman Kodak Co., CCH Trade Reg. Rep.* ¶25,291 (10th ed., 1955). To satisfy administration objections he consented to the amendment "in order that there may be no misunderstanding. . . ." *Ibid.*

At least two alternative interpretations may be suggested for the important proviso concerning horizontal arrangements. If it is designed to insure that the *immunity extended is limited strictly to vertical* minimum price fixing, the horizontal agreements of which it speaks

Recognizing that resale price maintenance is a "privilege restrictive of a free economy,"<sup>17</sup> the Supreme Court has limited the immunity granted by Miller-Tydings through a strict construction of that Act.<sup>18</sup> The Court employed this approach in *United States v. McKesson & Robbins, Inc.*,<sup>19</sup> a suit for an injunction against price fixing in violation of Section 1 of the Sherman Act. The defendant set up the Miller-Tydings Act as a defense, and the issue turned on the application of that act to an integrated manufacturer. McKesson, the largest drug wholesaler in the country,<sup>20</sup> had 1954 sales totaling

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may be assumed to be among those already within the condemnation of the Sherman Act. The meager legislative history available (*supra*) supports this alternative. If, however, it attempts to *limit the immunity granted to vertical* minimum price fixing in situations where such price fixing is associated with a horizontal agreement, the specified horizontal agreements may not only be those which violate the Sherman Act, but any horizontal minimum price fixing agreement. Though the less likely, this latter interpretation may be defended. The Act does not refer to that kind of horizontal price fixing which was illegal at the time the Act was passed because of an absence of any mention of market significance—a necessary concomitant of the illegality of horizontal agreements, at least until the Socony case (note 5 *supra*) several years after Miller-Tydings. Then too, while its language, "the preceding proviso shall not make lawful," suggests that the prohibition proviso is not seeking to create any standard of illegality with respect to horizontal agreements, it has been read by the Supreme Court as an affirmative enactment. The prohibition, it is said, "expressly continues the prohibitions of the Sherman Act against 'horizontal' price fixing by those in competition with each other at the same functional level." *Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U.S. 384, 389 (1951).

The choice between these alternatives would be decisive only where the market significance of a horizontal agreement was so slight that it would be unlikely to offend the so-called *per se* illegality of such agreements under the Sherman Act. The possibility of such alternative interpretations has not been acknowledged by the Court, perhaps because no case has arisen under Miller-Tydings involving a horizontal agreement not in violation of the Sherman Act.

<sup>17</sup> *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305, 316 (1956).

<sup>18</sup> E.g., *Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U.S. 384 (1951) (Miller-Tydings Act does not save from unconstitutionality state statute purporting to bind non-signers); *United States v. Univis Lens Co.*, 316 U.S. 241 (1942) (seller of unfinished article cannot impose resale price maintenance). See *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707, 721 (1944): "A distributor of a trademarked article may not lawfully limit by agreement, expressed or implied, the price at which or the persons to whom its purchaser may resell, except as the seller moves along the route marked by the Miller-Tydings Act."

In the state courts the constitutionality of fair-trade legislation has been challenged with increasing success. *Dr. G. H. Tichenor Antiseptic Company v. Schwegmann Brothers Giant Super Markets*, 231 La. 51, 90 So.2d 343 (1956) (non-signer provisions of Louisiana fair-trade act held an unconstitutional delegation of legislative power to the contracting parties, and also a violation of due process provisions of state and federal constitutions), where the court lists cases since 1952 holding fair-trade legislation unconstitutional in twelve states (Arkansas, Colorado, Florida, Georgia, Indiana, Kentucky, Michigan, Nebraska, Oregon, South Carolina, Utah, and Virginia), and upholding its constitutionality in nine (California, Delaware, Maryland, Massachusetts, New Jersey, New York, Ohio, Pennsylvania, and Wisconsin).

<sup>19</sup> 351 U.S. 305 (1956) (Justices Harlan, Frankfurter, and Burton, dissenting), *rev'g* 122 F. Supp. 333 (S.D. N.Y., 1954).

<sup>20</sup> Transcript of Record, at 141, *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305 (1956) (henceforth referred to as "Record").

338 million dollars,<sup>21</sup> including 11 million in "McKesson brand products" produced in its own manufacturing division.<sup>22</sup> It was organized into one manufacturing and seventy-four wholesale divisions, each an autonomous organization responsible only to the corporation's president and directors.<sup>23</sup> McKesson brand products reached the consumer through four channels of distribution: (1) 7 per cent through sales by the manufacturing division to independent wholesalers whose trade areas were "substantially identical or materially overlapping" with those of McKesson wholesale divisions (5 per cent) or who sold in competition with the direct sales by the manufacturing division (2 per cent);<sup>24</sup> (2) 13 per cent through direct sales by the manufacturing division to large retailers;<sup>25</sup> (3) 78 per cent through sales by the wholesaling divisions to retailers in trade areas "substantially similar or materially overlapping" those of independent wholesalers of McKesson brand products (7 per cent), and in trade areas where the competition of the independents was not present (71 per cent);<sup>26</sup> (4) 2 per cent through sales by the wholesaling divisions to independent wholesalers serving the same trade areas as those divisions.<sup>27</sup>

After 1951 all of the McKesson products were sold under agreements by which the buyer agreed not to resell at less than the "[m]anufacturer's published wholesale [or retail] prices."<sup>28</sup> Contracts with wholesalers and direct-sale retailers were solicited by the manufacturing division<sup>29</sup> and signed by one of its officers.<sup>30</sup> Shipment was made from, and the payment remitted directly to, the manufacturing division.<sup>31</sup> Pursuant to McKesson's policy that its wholesale divisions have nothing whatever to do with independent wholesalers, none of those divisions participated in any of the price maintenance,<sup>32</sup> nor were the McKesson wholesalers bound to conform to the stipulated wholesale prices.<sup>33</sup> Since they contracted with respect to all of McKesson's brands, however, the independents were bound as well for that which they bought from the wholesale as from the manufacturing divisions.<sup>34</sup>

The complaint sought to declare illegal and enjoin a combination and conspiracy between McKesson and the independent wholesalers to fix minimum wholesale and retail prices.<sup>35</sup> No permanent relief was sought against McKesson's price maintenance contracts with retailers.<sup>36</sup> The Government's

<sup>21</sup> Record, at 140.

<sup>22</sup> *Ibid.*, at 66.

<sup>23</sup> *Ibid.*, at 31, 36, 70, 72.

<sup>24</sup> \$763,767.00. (All figures for fiscal year ended June 30, 1952.) Record, at 30; Brief for Appellant, at 8-9.

<sup>25</sup> \$1,352,521.00. Brief for Appellant, at 7.

<sup>26</sup> \$8,306,672.00. Record, at 31.

<sup>27</sup> \$200,000.00. Record, at 56-57. These sales were said to be "principally of a courtesy nature" to allow other wholesalers to fill demands for McKesson products. *Ibid.*, at 55.

<sup>28</sup> *Ibid.*, at 206, 208.

<sup>29</sup> *Ibid.*, at 207, 209.

<sup>30</sup> *Ibid.*, at 56.

<sup>31</sup> *Ibid.*, at 56.

<sup>32</sup> *Ibid.*, at 54-55.

<sup>33</sup> *Ibid.*

<sup>34</sup> *Ibid.*, at 57-58.

<sup>35</sup> *Ibid.*, at 1-4.

<sup>36</sup> The complaint did seek to enjoin "inducing, persuading or causing" retailers to observe minimum resale prices "for such time as is necessary to dissipate the effects of the aforesaid combination." *Ibid.*, at 4.

motion for summary judgment was denied,<sup>37</sup> and after its evidence had been presented the complaint was dismissed by the district court for failure to prove some "additional restraint of competition . . . which, in conjunction with their fair trade price fixing, would constitute a violation of the Sherman Act."<sup>38</sup>

In reversing, the Supreme Court took a simplified view of the case.<sup>39</sup> The Court reasoned that price fixing is illegal per se unless immunized by Miller-Tydings and that the McKesson contracts with independent wholesalers were not immunized since they fell within the proviso in that they were

*between wholesalers, or between brokers, or between factors, or between retailers, or between persons, firms, or corporations in competition with each other.*<sup>40</sup> [Emphasis by the Court.]

The plain implication of this decision is that any integrated firm engaging in resale price maintenance with firms performing the same distributive functions (at least in the same market area) is in violation of Section 1 of the Sherman Act.<sup>41</sup> Since a large percentage of fair-trade manufacturers are partially

<sup>37</sup> *United States v. McKesson & Robbins, Inc.*, 122 F.Supp. 333 (S.D. N.Y., 1954).

<sup>38</sup> Record, at 182.

<sup>39</sup> The Court declined to consider the "unedifying and unilluminating" legislative history since "the language of the proviso in question is unambiguous." *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305, 315 (1956).

<sup>40</sup> *Ibid.*, at 311, quoting the Miller-Tydings Act, in text at note 16 supra.

The Court raised but did not answer the question of whether "in competition with each other" modified each of the suggested combinations or only the last, since its reliance was placed primarily on the last category; and if a wholesaler, McKesson was in any event competing with those with whom it had fair-trade contracts. *Ibid.*, at 312. To this point the opinion states: "Congress thus made as plain as words can make it that, without regard to categories or labels, the crucial inquiry is whether the contracting parties compete with each other. If they do, the Miller-Tydings and McGuire Acts do not permit them to fix resale prices." *Ibid.*, at 313. From this language the decision may be regarded at the same time as an extension and restriction of fair trade. It seems to indicate that whether or not a manufacturer has a "wholesale division" it will be prohibited from price maintenance with independent wholesalers if it "competes" with them in the same market area by performing similar functions, as by making direct sales to retailers. Conversely, fair-trade contracts by a manufacturer would seem legal if its wholesale functions are separately incorporated, as then the "contracting parties" would not compete. Cf. *Eastman Kodak Co. v. Schwartz*, 133 N.Y.S.2d 908, 919, 925 (S. Ct., 1954), discussed in note 44 infra, where the court relied on the separate incorporation of the manufacturer's retailing facilities in enforcing its fair-trade contracts.

<sup>41</sup> For the integrated manufacturer the decision poses a choice between fair trade and integration. Eastman Kodak and Miles Laboratories have already chosen the latter by cancelling their fair-trade contracts.

In seeking to avoid the decision a manufacturer might incorporate its wholesale facilities, enter fair-trade contracts with them, and then attempt to hold independent wholesalers under the non-signer provisions. But the courts would likely treat a manufacturer who can force independents to adhere to his designated resale prices as if he actually had contracted with them. Once this step is taken the McKesson case is direct authority.

integrated,<sup>42</sup> the case severely diminishes the coverage of fair-trade legislation. But such a reduction should not be made by mechanical application of a statute which undoubtedly was passed without regard to the particular problem of the integrated manufacturer.<sup>43</sup> That alternative approaches are available is indicated by an examination of other opinions dealing with the same problem.<sup>44</sup>

In *Eastman Kodak Co.*<sup>45</sup> the Federal Trade Commission considered a complaint for price fixing brought against a leading manufacturer of photographic supplies whose subsidiaries maintained thirty-five retail outlets selling Eastman products in competition with the retailers to whom Eastman made direct sales and with whom it entered the questioned price-maintenance con-

<sup>42</sup> A recent sampling of fair-trade manufacturers indicated that approximately 75 per cent were partially integrated. *Eastman Kodak Co.*, 3 CCH Trade Reg. Rep. ¶25,291 n. 25 (10th ed., 1955).

<sup>43</sup> The only mention of the application of fair-trade legislation to the integrated firm came during Senate debate of the McGuire Act. Stating that the source of illegality of resale price agreements was the absence of the buyer-seller relationship, Senator Humphrey concluded that integrated firms could enter such agreements "when in making such contracts, they act as producers . . . rather than as wholesalers or retailers entering into forbidden horizontal resale price maintenance contracts with other wholesalers and retailers." 98 Cong. Rec. 912 (1952). The Court in *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305, 313 n.17 (1956), quotes the entire statement and discounts it because Humphrey was neither in charge of the bill nor on any committee that had considered it, and because when he spoke the bill had already been passed by the House.

<sup>44</sup> In addition to the authorities discussed in the text, most courts which have considered the issue have approved resale price maintenance by the integrated firm. In *Eastman Kodak Co. v. Schwartz*, 133 N.Y.S.2d 908 (S.Ct., 1954), the court enjoined the defendant non-signer from disregarding the plaintiff's designated resale prices, after rejecting the contention that plaintiff's fair-trade contracts were invalid because between a manufacturer-retailer and competing retailers. Relying on the express language of the McGuire Act, its legislative history, and the fact that the retailing subsidiary was an entity distinct from the parent manufacturer, the court found that Eastman had acted in its capacity as a manufacturer so that the contracts fell within the protection of the fair-trade statutes.

Several cases contain dicta approving the use of fair-trade contracts by integrated firms. See *Razor Corp. v. Goody*, 121 N.Y.S.2d 882, 886 (S.Ct., 1953) (sale of similar products in different parts of the world by parties to a fair-trade agreement not of itself "sufficient to establish proof of any competition and consequently an illegal horizontal agreement"); *Sunbeam Corp. v. Payless Drug Stores*, 113 F.Supp. 31, 39 (N.D. Cal., 1953) ("there is no indication in the Miller-Tydings Act itself or in its legislative history that Congress intended to . . . alter established systems of distribution in order [for a manufacturer] to avail himself of the benefits of the Act."); *Gillette Safety Razor Co. v. Green*, 167 N.Y. Misc. 251, 252, 3 N.Y.S.2d 822, 824 (S.Ct., 1938) ("nothing in the law to prohibit a manufacturer or producer from selling both wholesale and retail"). But see *General Electric v. S. Klein-on-the-Square, Inc.*, 121 N.Y.S.2d 37 (S.Ct., 1953) (integrated manufacturer could not make fair-trade agreements with other wholesalers and retailers).

There are also several cases involving integrated firms in which that fact either was not raised or was given no significance. E.g., *Old Dearborn Distributing Co. v. Seagram-Disstillers Corp.*, 299 U.S. 183 (1936); *General Electric Co. v. R. H. Macy & Co.*, 199 N.Y. Misc. 87, 103 N.Y.S.2d 440 (S.Ct., 1951); and *Doubleday, Doran & Co. v. R. H. Macy & Co.*, 269 N.Y. 272, 199 N.E. 409 (1936).

<sup>45</sup> 3 CCH Trade Reg. Rep. ¶25,291 (10th ed., 1955).

tracts. Of the total sales of Eastman's fair-traded products,<sup>46</sup> its company-owned stores sold less than 3 per cent.<sup>47</sup> In determining whether these contracts came within the protection of the fair-trade legislation, the Commission was powerfully influenced by the fact that many manufacturers are partially integrated, a fact of which the Commission felt Congress must have been aware. Not only was it unlikely that Congress intended to discriminate against partially integrated concerns, the Commission reasoned, but a decision that it had done so "would require thousands of manufacturers, if they want to fair trade, to make major changes in their present marketing methods with uncertain but admittedly large economic consequences."<sup>48</sup> So motivated, the Commission concluded that the fair-trade contracts were legal, using this test:

When negotiating the fair trade agreements with retailers was respondent acting in its capacity as a manufacturer . . . or in its capacity as a retailer? In other words, it is necessary to study the particular agreement, examine its form, economic purpose, intent and effect and then decide whether it is a vertical or horizontal . . . agreement.<sup>49</sup>

The Commission gave no particular insight into what considerations should be utilized in determining the capacity in which the defendant had acted in its price-fixing activities.

A similar disinclination to adopt a strict application of the statute was evidenced by the district court in the *McKesson* case in denying the Government's motion for summary judgment. The court reasoned that the statute would provide an easy solution only "if one of defendant's capacities is carefully considered and the other happily ignored."<sup>50</sup> Recognizing that the dual role of *McKesson* created a dilemma for the words of the statute, the court was unwilling, at this stage of case law development of legislatively sanctioned resale price fixing, to hold illegal *per se* fair trade agreements because the producer is also a wholesaler in the absence of showing some injury, inchoate or consummate, to competition.<sup>51</sup>

Dissenting in the *McKesson* case, Justice Harlan was even more generous to fair trade, proposing an approach under which the fair-trade contracts of

<sup>46</sup> In 1951 Eastman and its subsidiaries had total sales of \$542,824,000, of which \$111,737,000 (less than 21 per cent) were fair-traded. *Ibid.*, at p. 35, 418.

<sup>47</sup> The sales of company-owned stores totaled \$34,806,000, of which \$3,104,000 (about 9 per cent) represented fair-traded products. *Ibid.*

<sup>48</sup> *Ibid.*, at p. 35, 423-24. The Commission also relied on the legislative history (discussed at note 16 *supra*) and the decision of the district court in the *McKesson* case, discussed above.

<sup>49</sup> *Ibid.*, at p. 35, 420-21.

<sup>50</sup> *United States v. McKesson & Robbins, Inc.*, 122 F.Supp. 333 (S.D. N.Y., 1954).

<sup>51</sup> *Ibid.*, at 337.



both integrated and non-integrated manufacturers would be treated alike. In his view the extent of the immunity granted by the fair-trade laws should be determined by giving effect to the purpose behind those laws, which he found to be the preservation of manufacturer's goodwill, by allowing the elimination of price competition on the resale of its brands. Then he reasoned:

Certainly the integrated manufacturer has as strong a claim to the protection of his goodwill as a non-integrated manufacturer, and the economic effect of the contracts is the same. In both cases price competition in the resale of the branded product is eliminated, and in neither case does the price fixing extend beyond the manufacturer's own product.<sup>52</sup>

He avoided the contention that these contracts fell under the proviso by interpreting the function of that clause as insuring the maintenance of competition between brands.<sup>53</sup> Apparently assuming that resale price maintenance by an integrated manufacturer could effect no decrease in competition between brands,<sup>54</sup> he concluded that "an integrated manufacturer selling its products under fair-trade contracts to independent wholesalers should be deemed to be acting as a 'manufacturer' rather than as a 'wholesaler.'"<sup>55</sup>

Resale price maintenance by an integrated manufacturer occupies an area of uncertainty between the ban against price fixing and congressional approval of resale price maintenance. Although exhibiting a uniform distaste for a blanket prohibition of such contracts, none of the foregoing decisions offers a wholly satisfactory standard for resolving which should and which should not be illegal. The Federal Trade Commission proposal,<sup>56</sup> making the issue turn on the capacity in which the integrated firm had acted in executing the

<sup>52</sup> *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305, 318 (1956).

<sup>53</sup> "The vice of price-fixing agreements between those in competition with each other, whether at the manufacturing, wholesaling, or retailing level, is that they can be utilized to eliminate competition *between brands*." *Ibid.*, at 319. If Justice Harlan meant that the exclusive function of the prohibition clause was to protect competition between brands, his construction flies in the face of the statutory language "any commodity herein involved" (quoted in text at note 16 *supra*). Exclusive use of the singular strongly suggests that the prohibition is at least in part concerned with the elimination of price competition with respect to a single brand. Actually he vacillated on the foregoing point and several lines later intimated that since a contract between wholesalers with respect to a single brand was "unnecessary to the protection of goodwill" and thus "would serve no purpose other than the elimination of competition" it would be condemned. *Ibid.*

<sup>54</sup> But where the wholesaling facilities of an integrated manufacturer are devoted to the sale of non-fair-traded competing products it can sell these other brands at prices equal to those at which its own fair-traded products must be sold by its competitors, thus affecting an elimination of competition between competing firms with respect to different brands. Of course, confronted with industry competition such price-hiking could only be pursued by a firm in an oligopolist position. The necessity of size to bring about an effective elimination of competition in this manner suggests that the evil is not alone price fixing, but monopolizing as well.

<sup>55</sup> *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305, 319-20 (1956).

<sup>56</sup> Quoted in text at note 49 *supra*.

agreements, seems the most attractive if there is some objective standard by which this can be determined. It is tempting to use comparative sales figures. With McKesson & Robbins, for example, wholesale sales are thirty times manufacturing sales.<sup>57</sup> But the likelihood of dissimilar profit margins warns that the sales ratio is not necessarily an effective measure of the integrated firm's predominant economic interest. The relative amount of profit from either activity is also of questionable utility, resting as it does on perhaps debatable cost allocations and easily-rigged prices on intra-firm sales. It also seems unprofitable to attempt to determine the extent to which one function is performed only as an adjunct to another. For example, while it seems unrealistic to say that McKesson, the country's largest drug wholesaler, entered into price-maintenance contracts in other than that capacity, this common sense conclusion is not easily substantiated. The only approach which seems meaningful is to determine whether or not a manufacturer's performance of wholesaling functions gives him a sufficiently different economic interest in resale price maintenance with independent wholesalers so that he can be deemed to be "acting as a wholesaler."

Where the wholesale activities are limited to the firm's own product, its interests appear indistinguishable from a non-integrated manufacturer. It has no additional economic incentive for entering into resale price maintenance with independent distributors since its manufacturing division will pay the cost (in lower volume) for benefits (higher resale prices) which its wholesale division must share with the independents. Its only motivations for entering resale price maintenance, such as remunerating dealers for special promotional, distributive, or service activities, or preventing the elimination of outlets providing essential dealer services through undercutting by outlets which do not provide them, appear equally applicable to the non-integrated manufacturing firm.<sup>58</sup> Similarly, the price-maintenance contracts of either serve only to eliminate competition with respect to the subject brand. There appears to be no more justification for condemning the price-maintenance contracts of this integrated manufacturer than those of a non-integrated one.

Quite a different situation may be presented, however, where the wholesaling facilities are devoted to the sale of products competing with its own manufactures, as was the case with McKesson & Robbins. As a wholesaler the firm would want a price-fixing agreement with other wholesalers in order to maximize its revenue. Since a price-fixing agreement may break down unless it includes substantially all of the competing products, as a wholesaler the integrated firm has a strong interest in having the manufactured product

<sup>57</sup> Consult text at notes 21-22 *supra*.

<sup>58</sup> Bowman, *op. cit.* *supra* note 3, at 832-43, rejects the conventional protection-of-goodwill rationale for manufacturer-inspired resale price maintenance and concludes that only the above-named motivations have any substantial validity. Coercive action by distributors, another possible motivation, is illegal. *United States v. Frankfort Distilleries, Inc.*, 324 U.S. 293 (1945).

fair-traded. When the integrated firm's loss from fair-trading qua manufacturer is exceeded by its gain from wholesaling its own and other fair-traded goods qua wholesaler, this will tip the scales of its over-all interest in favor of resale price maintenance. In such a case the economic interest of an integrated manufacturer is not that of a non-integrated one but that of a wholesaler, and it can be said to be "acting as a wholesaler." Accordingly, its resale price-maintenance contracts should not qualify for immunity under *Miller-Tydings*.

Because the integrated firm's balance of interests will at least occasionally be that of wholesaler, and because it is impractical to require a court to weigh nicely the respective gains and losses from resale price maintenance to determine when that condition exists, where the wholesaling facilities of an integrated manufacturer sell competing brands this should be sufficient justification for regarding it as a wholesaler and condemning its participation in resale price maintenance.<sup>50</sup> Since the *McKesson & Robbins* wholesale division purchased and resold competing brands the result reached by the court is consistent with the foregoing analysis. But upon that analysis it is equally clear that despite its broad language the *McKesson* case ought not to be taken to condemn resale price maintenance by a firm which "compete[s]"<sup>60</sup> with those with whom it contracts only by performing similar functions solely with respect to its own manufactured products. Finally, the autonomous nature of the *McKesson* manufacturing division, and the care taken to assure that the price-maintenance contracts were negotiated and executed exclusively by that division<sup>61</sup> suggests that the decision is not to be avoided by a separate incorporation of the integrated facilities.

<sup>50</sup> The suggested analysis also offers a solution to the situation where the integrated firm is the wholesaling (or retailing), rather than the manufacturing, party to the contract. Since the wholesaling division of the integrated firm is handling the goods of other manufacturers it will be regarded as a wholesaler. If it enters into fair-trade contracts with a manufacturer whose integrated facilities wholesale the goods of other producers, the contract would be condemned as between wholesalers. If it enters into fair-trade contracts with a manufacturer who wholesales no goods, or no goods other than its own, the contract would be proper, as between a manufacturer and wholesaler. But compare the language of the Court quoted in text at note 40 *supra*, and in note 40 *supra*.

<sup>60</sup> Consult the language of the Court quoted in note 40 *supra*.

<sup>61</sup> Consult text at notes 29-33 *supra*.

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#### PENDENT JURISDICTION—APPLICABILITY OF THE *ERIE* DOCTRINE

Even in the absence of diversity of citizenship, a federal court may, under the doctrine of pendent jurisdiction,<sup>1</sup> allow joinder of a non-federal claim

<sup>1</sup> The term "ancillary jurisdiction" is sometimes used to describe those situations in which disputes involving state-created rights are adjudicated by federal courts in non-diversity cases. "Pendent jurisdiction" is used in this comment to refer to that ancillary jurisdiction